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SENSITIVE
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STATE FOR EEB/IFD/OMA
TREASURY FOR DO/IDD AND OUSED/IMF
SECDEF FOR USDP/DSCA
PASS EXIM FOR CLAIMS - MPAREDES
PASS USDA FOR CCC -- ALEUNG/WWILLER/JDOSTER PASS USAID FOR CLAIMS --
WFULLER
PASS DOD FOR DSCS -- PBERG

E.O. 12958: N/A
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SUBJECT: PARIS CLUB - MARCH 2008 DISCUSSION OF POLICY AND
METHODOLOGICAL ISSUES

Summary

¶1. (SBU) The Paris Club met on March 13 to discuss 16 countries and other policy and methodological issues. Creditors reported on contacts with the new Argentine government, which has been arguing against an IMF agreement and for minimizing external payments in seeking a Paris Club deal. The IMF's report on the DRC made clear that HIPC Completion Point will not be reached this year. On Cuba, creditors confirmed that they had not discussed medium- or long-term debt with Cuba; many creditors that had restructured short-term debt

with Cuba now found that Cuba was in arrears yet again. Russia announced the February signing of the bilateral agreement implementing its 2004 commitment to provide Iraq debt relief, while Brazil reported on contacts with Iraq's advisors. Liberia is on track to receive Paris Club interim HIPC relief in April, while Togo should receive a pre-HIPC debt treatment in May. The Club discussed a French idea to provide a type of "debt moratorium" for countries embarking upon Emergency Post Conflict Assistance (EPCA) programs. Several creditors noted the proposal would erode the principal of conditionality, while the U.S. and others raised possible legal impediments.

Argentina

¶2. (U) The IMF reported that there had been a February mission to discuss the effects of global volatility on Argentina, and that they continued to discuss inflation measurement issues. No date had been set for an Article IV. The World Bank reported that it was looking at a three-year program, likely to come to the Board at end-2008, of about \$1 billion/year. All of the proposed loans will be investment lending. The Bank has made no adjustment loans to Argentina since 2003 (adjustment loans are generally for budget support and imply some level of comfort with macroeconomic policy); the outstanding portfolio is about \$5 billion.

¶3. (SBU) Bilateral Contacts: The Secretariat/France, Germany, Italy, the UK, and U.S. all reported on various bilateral meetings with Argentine officials. They all reported holding to the Paris

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Club position that there can be no restructuring without an IMF agreement and that Argentina should resume payments. Argentine officials, in turn, had stated to France that their priorities were not to increase financing needs and not to challenge current stability and economic performance. The GOA aims to maintain reserves to guard against external shocks, and noted that there were both legal and policy constraints against using reserves. The GOA claimed it could not afford a voluntary settlement of arrears. France had not found this an acceptable justification and reminded the GOA of Club rules regarding conditionality. The Secretariat will initiate a data call in order to assess GOA data received recently. The Secretariat noted private banks regularly sued to avoid expiration of the statute of limitations on holdout bondholder claims.

¶4. (SBU) Germany reported GOA desire to resolve the issue in 2008; but the Argentines were "not eager" to resume payments, and they wanted better terms than the six-year schedule they had received from Spain, e.g., eight years. Germany also reported that the GOA had promised two items: statistical information, and a proposal by the end of March, ahead of the IMF/IBRD Spring Meetings. Germany had received a data presentation from Argentina (which the Secretariat distributed to all creditors). The Argentines had also

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proposed an IMF-type program -- perhaps even put together with IMF staff -- but issued instead by the Inter-American Development Bank (IDB), an idea that both France and Germany told Argentina was a non-starter.

¶5. (SBU) Finally, Italy reported no sign of an opening. For the time being, Argentina was defensive, made no indication of a payment as a goodwill measure, and claimed it could not afford to pay. The GOA had again said that the holdout issue had been settled by law and was not subject to reopening. Italy advocated insistence on a goodwill gesture compatible with the GOA's financial situation.

¶6. (SBU) The Netherlands asked the Secretariat to use its contacts to point out the need for payment as a goodwill gesture and to clear arrears, and suggested that Club members should refuse to engage until payments were resumed. The Secretariat disagreed, opining that Argentina should be allowed to make a proposal. All creditors agreed on the need for continued solidarity, and that the

Secretariat would prepare a new working paper before the Bank/Fund

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Spring Meetings, laying out a common message.

Congo (Brazzaville)

17. (SBU) The IMF reported that the new staff-monitored program (SMP) would be going to Management in mid-March and to the Board probably in June. The program would require cuts in subsidies and spending, and structural changes focused on public financial management and transparency. A May mission would review performance through March. The Bank reported that a recent HIPC progress mission had found mixed results, and that the PRSP would come to the Board by the end of July. The Fund also reported that Congo had signed three agreements with China, two of which are disbursing. The concessionality of one agreement --- for energy -- met PRGF requirements; the IMF had granted a waiver for the other agreement, which financed aircraft. There was also a 2006 framework agreement on priority sectors, including roads, airports, health and water, but it had not been activated; the IMF noted lack of clarity about projects covered and financing modalities. Neither the Bank nor the Fund had information about a recent agreement with litigating creditors, reported in the press. The Secretariat noted that reports had indicated that the agreement was above face value, and will write to Congolese authorities to inquire.

Democratic Republic of Congo (DRC)

18. (SBU) The Fund reported that the SMP was being extended for six months with a focus on corrective measures in public financial management, meaning that a PRGF could come no earlier than the summer, and Completion Point no earlier than 2009. Given the track record, this timetable is ambitious. November/December information revealed institutional weaknesses and fiscal deterioration, including unauthorized spending amounting to 2.5 percent of GDP. The central bank is establishing a committee in an effort to halt unauthorized expenditures. IMF staff will provide an update to the Club on DRC ability to make payments during the first half of 2008. A number of creditors expressed dismay at the delay, indicating that they would have to reallocate funding that had been intended for

DRC's debt treatment. Expressing concerns about debt sustainability and, more broadly, the impact of large PRC projects in Africa, creditors appreciated the IMF's work with DRC authorities. The Secretariat reported that the DRC had not responded to the

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Secretariat's October 2007 letter.

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Cote d'Ivoire

19. (U) The IMF reported higher than desired military spending and delays in implementing reforms. Despite the mixed performance under the previous EPCA, Cote d'Ivoire had requested a SDR 41 million follow-up, planned for April 4 Board discussion, that will focus on fiscal consolidation, cuts in non-priority spending, and investment in social infrastructure. A Poverty Reduction Strategy Paper (PRSP) is under preparation, and Decision Point could come later this year.

110. (U) There had also been progress in normalizing relations with creditors: Cote d'Ivoire was up-to-date with multilaterals and had settled much of its domestic debt. World Bank and African Development Bank (AfDB) arrears clearances were progressing, with the World Bank planning an April 1 Board date. European Investment Bank arrears clearance was also underway, and Cote d'Ivoire was

talking to London Club creditors.

¶11. (U) Paris Club creditors asked about litigating creditors. The Secretariat replied that discussions were ongoing, noting that

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private creditors were "not in a litigating mood" and appeared willing to provide HIPC-comparable treatment.

Cuba

¶12. (U) The Fund and Bank declined to report, on the grounds that Cuba was not a member. The Secretariat noted that the last discussions with Cuba (with a grouping of some creditors, not the Paris Club) had taken place in 2001, and that the country had not been discussed since November 2006. Creditors had agreed not to discuss medium- and long-term (MLT) debt with Cuba, but were free to seek agreements on short-term (ST) debt. All creditors indicated

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that they had adhered to this understanding.

¶13. (SBU) Countries reported as follows:

- o Canada: a July 2005 agreement on short-term debt arrears covered C\$13.5 million; there had remained a balance of arrears in short-term exposure. Since then, a June 2007 agreement on ST arrears covered C\$30.4 million, which had all been paid or were to be paid imminently. Canada's position was that there be no discussion of MLT debt.

- o Italy: there had been sporadic contacts, but no agreement on short-term debt, though both sides had reconciled most of the debt. ST claims were \$76.1 million, of a total exposure of \$290 million, plus an additional \$13 million in ODA.

- o Netherlands: had agreed a new payment schedule in 2004, which had gone off track. ST arrears were 19.7 million euros, principal not yet due 31 million euros. MLT debt was 2.4 million euros, plus an unspecified 1.1 million euro claim. No discussion of MLT debt.

- o Japan: had reached an agreement in 2000. ST claim was 13.2 billion yen, which was being honored promptly. Not covered was 6.5 billion yen, which was not in arrears. Arrears on MLT had been accruing since 1986, and totaled 154 yen billion as of March 2008. Japan had also been approached recently on MLT debt, but had declined to discuss it.

- o Spain: A mission in July 2007 had begun reconciliation of debts, a process which was close to completion. No ST negotiations had begun.

- o Russia: Indicated that it was the major creditor, with claims of \$25 billion as of early 2008. No progress had been made, even on reconciliation.

- o UK: had signed an MoU on ST debt in April 2003, totaling GBP 8.5 million. They had received three payments, but nothing since 2004.

- o Austria: had signed a bilateral in April 2002 covering 6 million euros, payments had been fairly regular, with the last due in

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December 2009.

- o Belgium: had signed an agreement rescheduling 12 million euros ST over five years. Since then, there had been no arrears, though some delays. There had been no request for discussion of MLT loans.

- o Germany: Agreement in May 2000. No arrears, no problems.

- o France: Short term debt totaled \$110 million, plus an additional 4 million euro in guarantees that had not been called. Working on

an ST agreement that should be reached in the near future.

o Switzerland: had signed an MoU in 2005 on SF45 million, which ends in August 2008. Has no MLT debt.

o U.S.: No discussions or agreement.

o Mexico: Italy and Spain reported that they had heard of a Mexico-Cuba agreement; Spain had heard it was for \$400 million.

Gabon

¶14. (SBU) Japan had asked for Gabon to be placed on the agenda, and it reported that Gabon had missed a 9.2 million yen payment on January 31. Three million yen of this had since been paid, but the rest remained outstanding. The U.S. reported that all arrears had been cleared; a number of creditors indicated that payments were frequently delayed or incorrect. Canada suggested that arrears to all creditors should be cleared before creditors moved forward on the buyback (a number have not yet implemented it), but the Secretariat opined that there were no arrears, only payment errors

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or technical arrears, and that no linkage was possible at this stage. Japan did not want repetition of this situation, in which debt buybacks occur even as Gabon fails to make scheduled payments. The Secretariat did agree to write to the Gabonese, which Japan accepted.

Haiti

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¶15. (U) The IMF reported that the second review of the PRGF had been completed, with one target missed and both spending and revenues below program targets. Creditors agreed to allow the second phase of Haiti's 2006 Paris Club agreement, conditioned on completion of the second review, to enter into force. A donors conference is set for April 25 in Port au Prince.

Iraq

¶16. (SBU) The U.S. had arranged with the Secretariat to have the Iraq discussion while Brazil was present in view of Brazil's failure to conclude a bilateral. The Secretariat pressed hard, noting that Brazil was one of the countries that had received an official letter from the Club, and asking what the problems were. The Brazilian delegate reported that there had been an unofficial meeting in Brazil with Iraq's advisors the previous week to discuss reconciliation of figures, and there could be another meeting in April or the beginning of May. The advisors had told Brazil that there was a June 3 deadline. Brazil said it would reply to the letter. The Secretariat reiterated the need to sign an agreement on Paris Club-comparable terms.

¶17. (U) The Russian delegate reported on the belated signing of Russia's bilateral. He agreed to provide a copy to the Secretariat, as required by standard Club procedures. The Secretariat agreed to share the bilateral with interested creditors.

¶18. (SBU) The Secretariat also indicated that it had met with Tunisia, which had declared its claims, to explain comparable treatment. Tunisia had begun discussions with Iraq. Algeria confirmed that it had claims, but had not done so by the deadline last year. The Secretariat had not yet met with Algeria to discuss comparability of treatment. The Secretariat also agreed to send new letters to Greece and Poland (which were not included in the most recent batch since they had received letters two years prior). In response to a question from the Netherlands on whether the Secretariat had raised the issue with Greece and Portugal on the

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margins of EU meetings as agreed, the Secretariat replied that no suitable meetings had taken place. Other EU members noted there

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were EU meetings every day. The Secretariat promised to raise the issue in the near future; if such an informal approach fails, the Secretariat will send letters. The Secretariat promised an update

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on this issue before the next Paris Club meeting. Japan inquired about China, noting that, at the January meeting, the Secretariat had wanted a schedule its technical meeting with PRC officials before sending a letter. The Secretariat reported that it was still finalizing the meeting with the Chinese.

Jordan

¶19. (U) Creditors participating in the buyback were asked about representation at the signing ceremony, and the Secretariat polled them on a Jordanian request for a date change. (The date reverted to the original March 30.) An IMF staff team was in Amman for Article IV discussions.

Liberia

¶20. (U) The Fund and Bank reported that their Boards were ready to approve Decision Point, accompanied -- in the case of the Fund -- by arrears clearance, restoration of voting rights, and the PRGF. The Secretariat will formally invite Liberia to negotiate on April 17.

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A few questions were raised about arrears to small multilateral creditors and about commercial debt negotiations. The IMF indicated total private debt in nominal terms is believed to be below \$2 billion, but because of lost or destroyed documentation, it is hard to determine the total amount.

Mali

¶21. (U) The IMF reported that agreement had been reached on a program, but that discussions had not been completed because some data outcomes had differed from expectations. Discussions would continue in late March. The IBRD reported on a new lending strategy and IDA/IFC program, cited no specific problems with the IDA portfolio, and noted some non-concessional borrowing from the Islamic Development Bank for electricity generation. The

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Netherlands reported growing arrears of 400,000 euros on a 4 million euro loan, while France reported 15 million euros in arrears. As a post-Completion Point HIPC, Mali has no formal relations with the Club. The Secretariat, however, promised to send an informal message to the authorities.

Serbia/Kosovo

¶22. (SBU) The Secretariat reported that Serbia was continuing to pay the portions of debt notionally allocated to Kosovo. The IMF's next visit to Serbia would be April 1. The World Bank indicated that Serbia had deposited enough money to cover three years of payments due to it, but excluding the putative Kosovar portion. However, Serbia had indicated that it still intends to pay the Kosovar share, which amounts to about \$500 million of \$2 billion. Many creditors reported that they had not yet signed agreements on the Serbia/Montenegro division of debt, although none raised particular concerns. The Netherlands reiterated its use of the debtor/guarantor, as opposed to final beneficiary, principle. On February 26, the U.S. signed its bilateral agreement with Montenegro. In a side conversation with the U.S., the Secretariat indicated that it had not received original loan documentation from

Serbia, notwithstanding GOS assertions to the contrary.

Seychelles

123. (SBU) The IMF said that the Article IV report had identified severe vulnerabilities, including sharp increases in arrears and debt ratios, and 27 percent inflation in January, but the Seychellois authorities had indicated that they needed more time to decide whether to seek a program. The Article IV had been delayed by "delicate" discussions on the exchange rate section. The Bank reported that a recent mission on debt management had found severe weaknesses, which the authorities did not seem to comprehend. The Secretariat reported a meeting with the Finance Minister, at which

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they had told him that a Fund program was necessary for Club treatment, and they felt that the Seychelles would seek one. The government has established a committee to look at new borrowing. The UK had pressed the President to seek a program. [The U.S. is

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not a creditor.]

Sudan

124. (SBU) The Secretariat asked Japan about recent reports that it had provided debt relief to Sudan. Japan explained, as it had privately, that the forgiveness under discussion dated from a 1978 Trade Development Board multilateral commitment at UNCTAD, which Japan understood most other Club creditors had delivered. Japan had decided to use the visit of Presidential Assistant Marfa to raise it as "simply a notification to deliver on a 1978 commitment." The relief, amounting to Yen 3.2 billion had not yet been delivered and was being tied to a number of prior actions, including efforts to end the Darfur conflict.

Suriname

125. (SBU) The IMF reported that growth was strong (6 percent in 2007, 7 percent projected for 2008) on the basis of commodity exports, with a doubling of reserves. The next Article IV discussion will be in May. The authorities had reported progress on arrears, including with Spain and the U.S., and that the GOS planned to negotiate with others. Brazil replied that it had in fact made little progress even in arranging a meeting in May. The U.S. reported the clearing of concessional debt arrears and the Surinamese request for reduction of non-concessional debt that remains in arrears. The Netherlands, in contrast, indicated that Suriname had repaid 70 million euros -- the entire balance of the GOS's outstanding ODA debt. The Secretariat stressed the importance of implementing the recent Working Paper on countries that had no relations with the Club, urging creditors to maintain a common position, not to deal bilaterally, and not to conclude agreements without reporting to the Club. Brazil requested a copy of the Working Paper, and the Secretariat asked to be kept informed of developments.

Togo

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126. (U) The IMF requested financing assurances for Togo's upcoming PRGF, scheduled for an early April Board date. The country's debt ratios will likely qualify it for HIPC, and a preliminary document could be ready in May or June, with Decision Point possible by year-end. World Bank and AfDB arrears would have to be cleared; the Bank reported that it would bring to its Board a plan to use an IDA grant to cover all of the arrears, and that it understood that talks with AfDB were well advanced. All creditors provided assurances (The U.S. requested a de minimus clause, since debt is just \$6,000.)

Negotiations are expected in May.

Vietnam

¶27. (U) Germany had requested that Vietnam be placed on the agenda and reported late payments. No other creditors reported late payments. The IMF reported that there had been a review in October, and that the main concern was overheating. The Bank reported that Vietnam had been declared creditworthy for IBRD lending and would be reclassified as a blend country, despite its low income level.

Methodological discussion:

Paris Club Treatment for Countries with EPCAs

¶28. (SBU) Creditors discussed a Secretariat proposal to provide treatment to IDA-only countries under Emergency Post Conflict Arrangements (EPCAs), namely to defer all payments during the EPCA period. The paper cited Iraq and Tsunami as precedents (Russia helpfully noted the understanding that Iraq was not to be used as a precedent for future Club action), and acknowledged departure from the Club's principle of requiring conditionality. The response was at best mixed, with numerous issues raised. Only France and Norway, while recognizing there was moral hazard, supported the proposal as written. Many, probably most, countries supported the principle, however, and felt the Club should keep pace with other institutions' efforts to lend support to fragile states. Sweden pointed out that the Club was a creditors group, not a development entity, an argument the Netherlands and Finland supported, and that this matter involves political decisions. Several countries argued the Club should await IMF deliberations on fragile states before acting. The

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U.S. indicated that it might have more general legal and budgetary constraints that could prevent it from participating.

¶29. (SBU) Japan argued that decisions should be made on a case-by-case basis to avoid providing relief to serial EPCA countries; the Secretariat and some others agreed. Italy asked what advantages there would be for HIPCs, whose debts would eventually be written off, and Belgium suggested inclusion of non-IDA countries. The UK, supported by Italy, asked how comparable treatment would be sought from other creditors, or whether it would be waived. The U.S. asked why France/the Secretariat saw this policy as necessary, since debts of EPCA

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countries had always been dealt with once the countries received upper credit tranche programs, and few, if any, affected countries would likely make payments during the EPCA. Spain's main concern was lack of conditionality and negative incentive effect, and legal issues for some creditors, and suggested linking treatment to a later PRGF by cancelling it if the PRGF were not reached. The Secretariat's reacted somewhat positively. The U.S. then made an

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alternative proposal, under which the Secretariat would send a letter to EPCA countries, noting the Club's understanding that arrears could continue to accumulate during the EPCA period and that the Club could be willing to address them when an upper tranche treatment were approved.

¶30. (SBU) Concluding the discussion, the Secretariat agreed to revise its paper, taking into account the Fund's discussions and the many comments made. It promised that the revised paper would be less didactic, but opined that there would be a political imperative for the Club to take some action.

Methodological discussion:

Relationships with China

¶31. (U) The Chinese Ministry of Trade had indicated that it was amenable to meeting with the Secretariat, although there had been no response from the Ministries of Finance and Foreign Affairs. The

meeting with Trade Ministry officials would take place in Beijing, probably at the end of March. The PRC prefers a technical meeting only with the Secretariat; representatives from Club member

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embassies would not be invited. At creditors' request, however, the Secretariat agreed to provide a readout to missions in Beijing. (On

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March 21, the Secretariat informed us that the technical meeting would take place on March 31; Embassy reps would be briefed on April 1.)

132. (U) A broader follow-up meeting could take place in Paris if the Chinese agree; the meeting would be billed as a "seminar," and other emerging market creditors would also be invited. The Chinese have not responded to this proposal.

Methodological discussion:
Paris Club Annual Report

133. (U) Creditors generally supported the Secretariat's plan for an Annual Report, a draft of which the Secretariat plans to submit for approval at the May Tour d'Horizon, for publication in June. Spain and Germany offered to be examples for the section on bilateral creditor efforts; others -- including the UK, U.S. and Japan -- suggested that the section be deleted, which the Secretariat agreed to do for this first annual report.

Methodological discussion:
Comparability of treatment - follow-up

134. (U) Creditors approved the letters the Secretariat proposed to send to debtors asking for information on their efforts to seek comparable treatment from non-Club creditors. The Secretariat also agreed to provide six-month updates on the results of these efforts.

STAPLETON